A Study on the Relationship between Foreign Ownership and the Performance of Chinese Listed Companies

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ABSTRACT

Besides dramatic increases of foreign direct investment in China, foreign ownership in Chinese companies still has artificial barriers and limitations in terms of accessibility and controllability in domestic companies. The doubtful questions that still exist are how and where the foreign ownership can contribute significant benefits to the corporate performance improvement of Chinese firms under the government's discriminatory treatment and strained stock market accessibility.

In respect to a call for better understanding, this study is aimed at providing a preliminary discussion about the relationship between foreign ownership and the performance of Chinese listed companies. The factors include foreign ownership, listed periods, economic size of listing companies, degree of financial leverage, and the performance of effectiveness and efficiencies. The data is collected from annual reports of listed companies in China from 2000 to 2004. A total of 50 companies with foreign ownership in the Shanghai Stock Exchange Market are chosen. The data analysis methodology used is descriptive statistics and multiple regressions. The proxies of each factor are the proportion of foreign ownership, listed years, sales income and debt to assets ratio, return on assets ratio and return on equity ratio.

This paper offers a conclusive definition for the present that there is no significant relationship between foreign ownership and the performance of Chinese listed companies. Foreign ownership has the claims over assets of invested companies but no or limited voting rights over strategic decision making. In order to be listed on the Chinese "B" share market and avoid investment withdrawal by foreign ownership, and other pressure, Chinese listed companies have to improve their internal management systems and standardize their management. However, this improvement is under the supervision of majority state share holders. Social stability is still the first consideration.

บทคัดย่อ

จากการที่ธุรกิจต่างๆ ในสาธารณรัฐประชาชนจีนมีการลงทุนจากต่างชาติเพิ่มขึ้น การร่วมลงทุนจากต่างชาติยังคงประสบปัญหา อุปสรรคและข้อจำกัดต่างๆ ในการเข้าถึงและควบคุมการดำเนินงานของธุรกิจดังกล่าว ปัญหาที่สำคัญ คือ วิธีการและแหล่งที่นักลงทุนสามารถเพิ่มผลประกอบการต่อการปรับปรุงการดำเนินงานของธุรกิจภายในสาธารณรัฐประชาชนจีน

การศึกษาวิจัยในครั้งนี้จึงได้จัดทำขึ้นเพื่อเป็นข้อมูลต่อการสร้างความเข้าใจในปัญหาดังกล่าว โดยมุ่งประเด็นการศึกษาไปยังการหาความสัมพันธ์ระหว่างการร่วมลงทุนจากต่างชาติและการดำเนินการของบริษัทต่างๆ ในสาธารณรัฐประชาชนจีน ตัวแปรที่ศึกษา ประกอบด้วย การร่วมลงทุนจากต่างชาติ ช่วงเวลาการดำเนินกิจการของบริษัทที่ศึกษา ขนาดของธุรกิจที่เป็นกลุ่มตัวอย่าง ระดับอิทธิพลทางการเงิน ประสิทธิภาพและประสิทธิผลของการดำเนินงานของบริษัทที่กลุ่มตัวอย่าง กลุ่มตัวอย่างที่ใช้สำหรับการทำวิจัยในครั้งนี้ คือ บริษัทที่มีการร่วมลงทุนจากต่างชาติในตลาดหุ้นของเซี่ยงไฮ้ จำนวนทั้งสิ้น 50 บริษัท โดยข้อมูลที่เก็บรวบรวมได้ถูกนำมาวิเคราะห์โดยใช้วิธีการทางด้านสถิติ ได้แก่ สถิติเชิงพรรณนาและการวิเคราะห์การถดถอยเชิงซ้อน

ผลสรุปที่ได้จากการทำวิจัยในครั้งนี้ พบว่า การร่วมลงทุนจากต่างชาติและการดำเนินการของบริษัทต่างๆ ในสาธารณรัฐประชาชนจีนไม่มีความสัมพันธ์กันอย่างมีนัยสำคัญทางสถิติการร่วมลงทุนจากต่างชาติมีอิทธิพลต่อสินทรัพย์ของบริษัทที่ถูกร่วมลงทุน แต่ไม่มีอิทธิพลต่อกลยุทธ์การตัดสินใจของบริษัทนั้นๆ ดังนั้น การได้มาซึ่งส่วนแบ่งทางการตลาดและการหลีกเลี่ยงการปฏิเสธการร่วมลงทุนจากต่างชาติ รวมทั้งปัญหาและอุปสรรคอื่นๆ บริษัทที่ถูกร่วมลงทุนควรมีการปรับปรุงระบบการบริหารงานภายในและมาตรฐานการจัดการต่างๆ อย่างไรก็ตาม การปรับปรุงดังกล่าวนี้ควรอยู่ภายใต้การตรวจสอบของผู้ถือหุ้นต่างๆ ในบริษัทรวมทั้งการให้ความสำคัญต่อเสถียรภาพทางด้านสังคมเป็นสำคัญ

INTRODUCTION

Since the initiation of economic reforms in 1979, China has become one of the world's fastest-growing economies (Morrison, 2005). Two major government policies are among the stimulating factors which have contributed to this achievement. First, the state allows the growth of the private sector and the township and village enterprises (TVEs) to participate in the economic restructure system (Chu and Tally, 2003). Second, the state promotes and encourages foreign investment first from direct regimes such as Hong Kong and Taiwan, to participate in the economy and allows the forming of foreign joint ventures, and even issuing tradable shares to foreigners (Zhang and Zheng, 1998). These two major policies allow private and foreign investors to purchase shares in State-owned Enterprises (SOEs) which is a major component of the Chinese economy.

When private firms purchase shares from State-owned enterprises (SOEs), the shares they hold are legal entity shares and called "A" shares. When foreign investors purchase shares of State-owned enterprises (SOEs), those shares have been classified as "B" shares in the Chinese stock market. The Chinese government allows foreign investment to acquire shares of a special category, B shares, of approved list companies in the Stock Exchange. However, ownership and management are separated. B shares only have claims on the assets and dividends of the companies but have no rights of decision making for the companies' management. The Chinese government is considering allowing foreign invested entities in China to be listed in the Stock Exchange, but it takes time for the government to come to this decision (China Securities Commission, 2003). It is believed that both private and foreign owners that hold "A" shares and "B" shares respectively have an impact on the corporate performance of Chinese listed companies.

In terms of impact from "A" shares", Qi, Wu and Zhang (1999) demonstrated that corporate performance is positively related to the proportion of "A" shares. Parker (2000) issued the same research result that Joint venture firms dominated more by "A" shares are more profitable. Wu (2004) presented that "A" shares can exert a monitoring effect and successfully lead the firm towards better performance. Those mentioned researches combined with many other issues make it obvious that "A" shares have a positive impact over corporate performance of Chinese listed companies which mostly are State-owned Enterprises (SOEs).

Then, there is an unsolved question. Whether foreign ownership participates in Chinese firms also has an impact on corporate performance? In other words, is there any relationship between foreign ownership and the performance of Chinese companies?

Based on general understanding, foreign investment as ownership should have an impact on the performance of Chinese companies. Existing research tells us that foreign investment is beneficial to the needs of the companies' strategic restructuring in emerging countries. First, it is believed that foreign investment generates positive externalities to the domestic firms through a transfer of know-how and technology (Konings, 2000). Second, companies with foreign ownership must improve their management systems in order to match the requirements from agencies if companies want to issue "B" shares to foreigners. Further more, it is also apparent that foreign investments really contribute strong fund availabilities to Chinese companies and probably benefit Chinese companies through oversea selling and business communications. All these stimulations should be considered as positive forces to improve the corporate performance of Chinese companies.

Nevertheless, there are different situations in China in which a majority of the economy is dominated by State-owned Enterprises (SOEs) which possess characteristics including large size, operational inefficiency, and financial distress (Chu and Tally, 2003). With the advent of globalization and economic growth, State-owned Enterprises (SOEs) became more and more a heavy burden for China. By 1997, China's traditional State-owned enterprises were producing only 25% of the gross value of industrial output while employing 33% of the industrial workforce and receiving 52% of total investment in fixed assets (Parker, 2000). These declines are determined by some fatal weaknesses. First, managers have no or little incentive to behave efficiently and to make profits for the enterprise because, considering China's current employment system, a manager's compensation had little to do with his or her performance in managing the company (Wang, 1997). Second, China opened capital markets to foreign investors since 1990s with the introduction of the "B" share in the Shanghai and Shenzhen Stock Exchange. However, severe agency problems arising from the separation of ownership and control continue to exist in these SOE-transformed companies if the state remains the controlling shareholders (Qi, Wu and Zhang, 1999). The state ownership has significant social burdens and goals such as providing retirement, healthcare, education, housing, and even jobs for employees' offspring that put them at a competitive disadvantage with other types of firms (Parker, 2000). But foreign investors consider highly the maximization of share values. With a limited proportion of capital they can invest in Chinese SOEs, those purposes have been restricted because of low percentage of voting rights (China Council for the Promotion of International Trade, 2004).

Consequently, foreign ownership in Chinese companies has an artificial barrier and limitation in terms of accessibility and controllability of domestic companies (Wang, 1997). The doubtful questions that still exist are how and where the foreign ownership can contribute significant benefits to the corporate performance improvement of Chinese firms under the government's discriminatory treatments and strained stock market accessibility. Even after obtaining ownership in Chinese firms by foreign investors, it is still uncertain that foreign ownership can result in a normal impact. This normal impact includes, an impact on the decisions of the companies, supervising authorities and so on, same as other major shareholders have. On the other hand, although the private ultimate controlled corporations are small at present, only 16% in 2001, it still raises a question that needs further scrutiny: is the current state-dominant shareholding structure in the Chinese public companies transitional or enduring? (Liu and Sun, 2003).

RESEARCH OBJECTIVES

The objectives of this study are to examine the relationship between foreign investment ownership and the corporate performance of Chinese firms. The study aims:

- To examine different performance results of the companies with different weight of foreign ownership.

SCOPE OF THE RESEARCH

This research study presents the relationship between foreign investment ownership and corporate performance of Chinese listed firms by using descriptive statistics and regression analysis. The data of the study was obtained from listed companies on the Shanghai Stock Exchange Market (SSE). The information can be implemented for most firms with conventional income statement and balance sheet data that are generally available in their annual reports to stockholders from 2000 to 2004. Considering the availability of the data, the study only adopts the annual data to make the investigation. The regression analysis is on the companies listed on the SSE except some listed companies under rehabilitation and investigation by government agencies or without foreign ownership.

There are some rationales for choosing the data starting from 2000 to 2004 for the study: the chances for foreign investors to invest in Chinese listed firms were very limited before. It was only in 1995 that control of a listed firm was sold. In July 1995, two Japanese firms, Isuzu and Itochu, purchased 40 million of the legal person (LP) shares of Beijing Light Bus. The premier, Li Peng, is reported to have accused the China Securities Regulatory Commission (CSRC) leadership of allowing foreigners to 'steal state assets' in this case, the further sales of LP were banned (Green, 2004). Except for this method of acquisition of shares, the only way for foreign investors is to purchase "B" shares in the Chinese stock market. However, the size and maturity level before 2000 still small and constrained as show in figures (China Securities Regulatory Commission, 2003).

Figure 1.4.1 B Share Market Summary 1 (1992-2004)

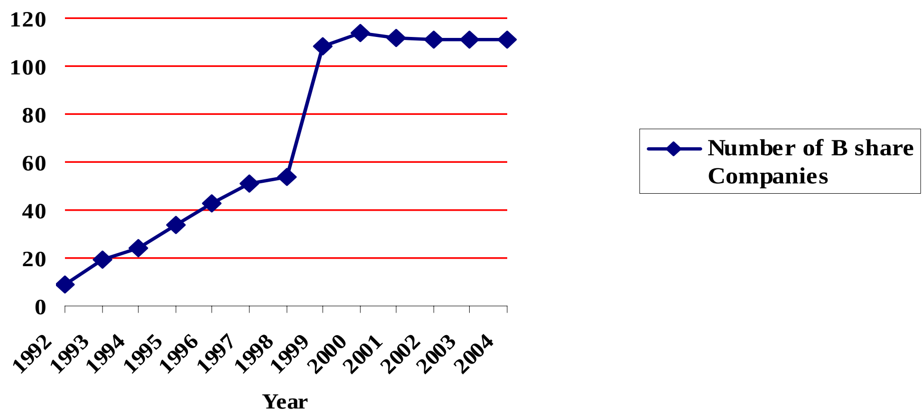
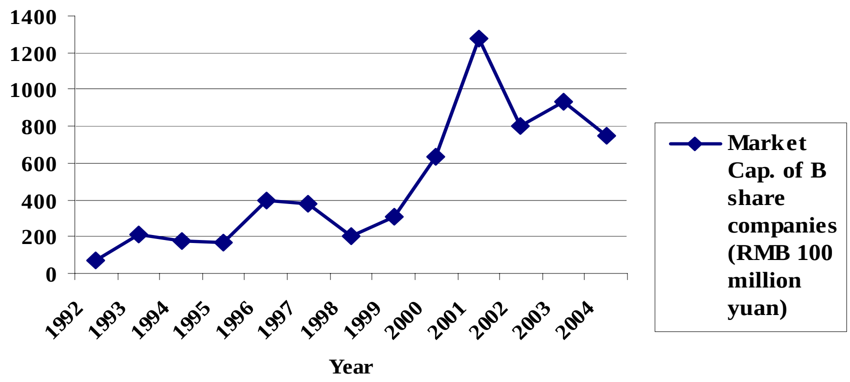


Figure 1.4.2 B Share Market Summary 2 (1992-2004)



Source: The Shanghai Stock Exchange Market (2005) (RMB: Chinese Currency, Ren Ming Bi)

THE ADOPTION OF RELATIVE LITERATURES FOR DEVELOPING THE RESEARCH FRAMEWORK

Chen and Demurger (1994) expressed that foreign direct investment exhibited higher productivity rates than their domestic-investment counterparts in the consumer goods industry. This research indicates the existence of impacts on performance of Chinese companies from foreign direct investment, even though just on the aspect of productivity. It makes us suspicious about, whether the overall performance impact from foreign investment exists beside productivity. This research employed technology, capital and labor as major variables in regression analysis. Those variables only reflect the productivity of Chinese companies, and can not express the whole story about the performance of Chinese companies. Consequently, their regression model will be only considered as a supportive indication in the study.

Konings (2000) adopted data from Bulgaria and Romania, Smarzynska (2002) used panel spanning over the period 1996-2000 to test the effect of direct foreign investment on domestic firms. These are good prompts and supports for this study in terms of indication and methods.

However, there are some limited points that need to be adjusted in the study. First, the same as Chen and Demurger (1994), these researches still concentrate on the output or productivity without considering more aspects of domestic companies. More broad explanations are urgently required by the present fast growth of the Chinese economy. Second, the Chinese market and economy were, and also are, much different from other emerging economies. Variables such as material inputs, labor, technology and even locations can be employed to detect production aspects of Chinese companies. But financing and efficiency of using all assets were not included in those models of regression analysis.

Fortunately, Zhang and Zheng (1998) gave a clear conclusion from the macro-view that MNEs have an impact on the Chinese economic structure. That indicates the existence of an impact if foreign investors are major shareholders or owners of companies. If foreign investors fully control companies, they focus more on the capital and knowledge intensive sectors. And it should be successful and more competitive. This leads us to the big question if there is any significant impact if foreign ownership is just one proportion of the Chinese companies which is not the same as MNEs absolutely controlled and owned by foreign investors?

Thanks to all the research mentioned above, there is a useful method we also can employ in the study. It is regression analysis. Under this method, some major variables which affect performance can be listed in the model. The model can tell us the relationship between foreign ownership and the performance of Chinese companies if other factors are hold as a constant such as economic size, listing age, financial leverage and so on.

The above mentioned research can contribute incentive and implication to this study. However, this study will more closely adopt Huang (2004), Qi, Wu and Zhang (1999), Wu (2004), and Xu and Wang (1997). There are some considerations for this adoption.

First, these four researches are relative to the relationship between ownership of state or legal person and performance. Then it is very rational if this study uses foreign ownership to replace other ownership in their models demonstrated after some adjustments have been made.

Second, except adopting these four methods, some adjustments should be made based on reality. Because foreign ownership development is quite different and special, based on the environmental and developmental background, the models and also variables used should be adjusted in this study.

AN IMPORTANT CONSIDERATION FOR DEVELOPING THE RESEARCH FRAMEWORK: FOREIGN OWNERSHIP IN CHINA

Let's look at the development and special characters of foreign ownership before analyzing its relationship with performance of Chinese companies.

Although the informal ban on non-tradable shares sales to foreign investors was out in place started from 1995, there are still some chances and methods for foreign investment to participate in Chinese companies. Based on the historical record and information, we can figure out and summarize the ways of investment from foreigners as follows:

The first method is acquisitions of large stakes in Chinese companies from outside the capital market. The foreign companies can make joint ventures with Chinese companies through Sino-Foreign Co-operative Joint Ventures, Sino-Foreign Equity Joint Ventures and Special Approved Foreign Joint Ventures. Under joint-venture, the foreign firms can buy out their listed Chinese partners for de facto controlling of the listed firm. Besides, the foreign investors also can be one of the owners of Chinese listed companies before Initial Public Offering (IPO) (Green, 2004).

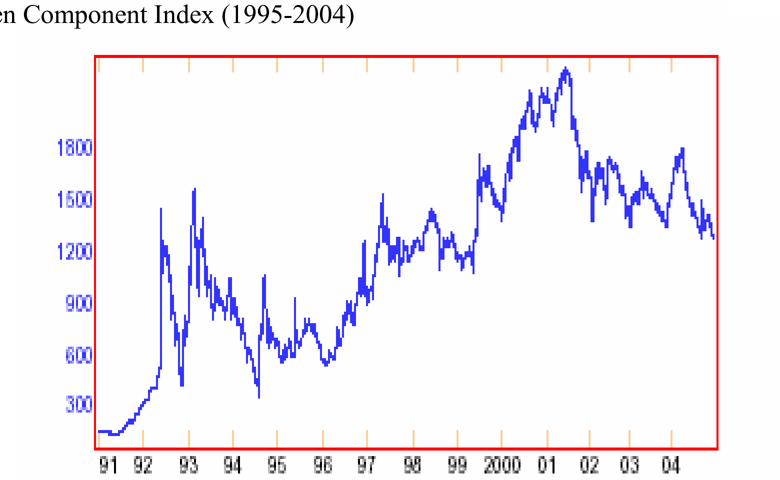
The second method can be explained as merging with other shareholders, such as Japan's Songgang Shushi Huishe and its merged subsidiart Terucom. After merger, the Japanese company took control of the shares of the third largest shareholder to take 41.7% of the listed company and become the first shareholder (Leung, et al, 2002).

However, in comparison with other Asian countries, China has distinctive features in the Stock Exchange Market that need foreign investors to understand.

Generally, there is a restrictive classification on the China Stock Exchange Market: State Shares hold by central or local government. Legal person shares refer to shares of a stock company owned by another company or organization. "A" Shares, also called individual shares refer to shares owned by Chinese residents (including domestic institutions), for a long time until recently it was traded among domestic investors at the two stock exchanges and was not accessible to foreign investors. "B" shares were originally offered exclusively to international investors and are denominated in RMB but were not permitted to be owned or traded by Chinese

Figure 3.1.1 Shanghai Composite Index (1991-2004)

Figure 3.1.2 Shenzhen Component Index (1995-2004)



Source: Shanghai Stock Exchange (2005)

citizens until 2001. The recent development of the Chinese stock market has been showed in figures. Oversea shares issued by Chinese companies listed on securities markets outside mainland China including H, N, L and S shares have been issued on the Hong Kong Stock Exchange, U.S. Stock Exchange, London Stock Exchange and Singapore Stock Exchange respectively (Mei, et al, 2004).

Apparently, there are only three types of shares for foreign investors that can be purchased in the public markets: "B" shares, oversea shares and "A" shares, "A" shares, however, only can be obtained recently. As the government is very aware of political consideration, access to ownership of Chinese companies is still tightly controlled.

As we knew, China's transition to a market economy has led to the development of several ownership identities, in a manner not typically found in Western European and North American firms. In order to maintain social stability and keep communist leadership in the economic system, the Chinese central government discriminates in the companies with state shares and legal shares, legal shares and foreign shares, through fund rising and tax policies and other government regulations in the Dual Regulatory System. Notwithstanding the resent liberalization of Chinese capital markets, foreign investors are still unable to participate in Chinese companies without limits.

THE RATIONALE OF THE FRAMEWORK

Based on previous research, ownership structure (both the mix and concentration) indeed has significant effects on the performance of listed companies. First, there is a positive and significant correlation between ownership concentration and profitability. Second, the effect of ownership concentration is stronger for companies dominated by legal person shareholders than for those dominated by the state. Third, firms' profitability is positively correlated with the fraction of legal person shares, but it is either negatively correlated or uncorrelated with the fraction of state shares and tradable "A" shares held mostly by individuals. Last, labor productivity tends to decline as the proportion of state shares increases (Xu and Wang, 1997).

Therefore, we believe that foreign investment participation can contribute significant improvement for corporate performance through owners' voting right executions if there are no authority pressures from the state. However, the real situation in Chinese listed companies is that a majority of shares are still kept in the state's hand, and foreign participation is restricted. Even the foreign participators hold relatively little higher shares with high reform desires still can not execute legal voting rights (Neih and Lu, 2004). The Directors just officially issue the information and decisions that have been made already at the shareholders conference.

Actually, as different ownerships have different social and benefit considerations, we have to say that the unavoidable contradictions among these types of ownership always exist in practice. State ownership considers social welfare and stability especially in the procedures of assets and raw materials procurement, employment, and other operations. Foreign owners look for maximization of share value. When conflicts incur, there are no negotiations and balances of the power.

In terms of legal shares, we found a majority of reconstructed shares belonged or do belong to the ex-state-owned institutions or corporations (Walter and Howie, 2003). It indicates that the companies with this type of legal shares are indirectly held by the state also. The inborn relationships and preconceptions will also limit the legal shares' abilities to maximize shares' value. Just as Qi, Wu and Zhang (1999) presented, the results based on 774 firm-years indicate that firms' performances, measured by the accounting rate of return on equity (ROE), decreases in the proportion of state shares, but increases in the proportion of other shares after controlling for size, leverage, industry, and the macroeconomic environment.

Then, under the current Chinese companies' ownership structure, the situation is complex. According to the preceding discussions, the companies with relatively high state ownership or ex-state-owned legal ownership will obtain privileges in fund rising and policy treatments because of own-baby consideration and protectionism from the central and local government. Consequently the companies with high foreign holdings but low state ownership will get uncertain answers to their companies' performance improvement.

THE THEORETICAL FRAMEWORK

Huang (2004) used markets to book, returns on assets as dependent variables and size, sales growth, leverage, age and fixed assets ratio to test the separation of ownership in the Chinese stock market. Qi, Wu and Zhang (1999) used returns on equity stands for performance and year, industry, size, debt to equity ratio as shareholding structure with control variables. Xu and Wang (1997) used return on equity stands for performance and year, industry, growth of net income, debt to equity ratio as affecting factors. To summarize it, the most frequently used factors are: size, financial leverage, industry, ownership, and age. But in terms of industry, there is no foreign "B" share in the conglomerates industry. According to that most companies come from the manufacturing industry and a limited number of listed companies for foreign ownership (totally 53), this study will not introduce industry to the model.

In a word, Chen and Demurger (1994), Konings (2000), Parker (2000), Smarzyns (2002), and Zhang and Zheng (1998), Wu (2004) used regression analysis to test the impact from foreign investment on Productivity and the economic structure of Chinese companies. Those findings can contribute significant prompts and desires to examine more broad impacts from foreign investment. They also tell that regression analysis is a useful way to help us find out desired solutions to research. However, because productivities and economic structure beside overall performance are focused in these studies, we will not mostly follow them. Other three researches from, Huang (2004), Qi, Wu and Zhang (1999), and Xu and Wang (1997) respectively, will be employed as major references for this study because their study on the relationship between ownership and performance of Chinese companies. Ownership in their studies was considered as state ownership or legal person ownership. We also can pretend this ownership is foreign ownership under the same methods they adopted.

As explained in the beginning of this chapter, the three researches from, Huang (2004), Qi, Wu and Zhang (1999), and Xu and Wang (1997), will be used as basic literature in this study. First, the regression model will be established for testing the relationship between foreign ownership and the performance of Chinese companies. Second, some variables used by these three previous researches for testing other ownership such as state and legal persons will be reconsidered in this study based on the background of foreign ownership in China mentioned in the beginning of this chapter. The basic variables listed in those researches can be summarized as that, ownership, industries, age, size, and financial leverage were used as independent variables and ROA, ROE and Market-to-book ration were used as dependent variables. However, Market-to-book rationale will not be adopted as an indication to test performance result from investors' confidence. The reasons are explained as follows.

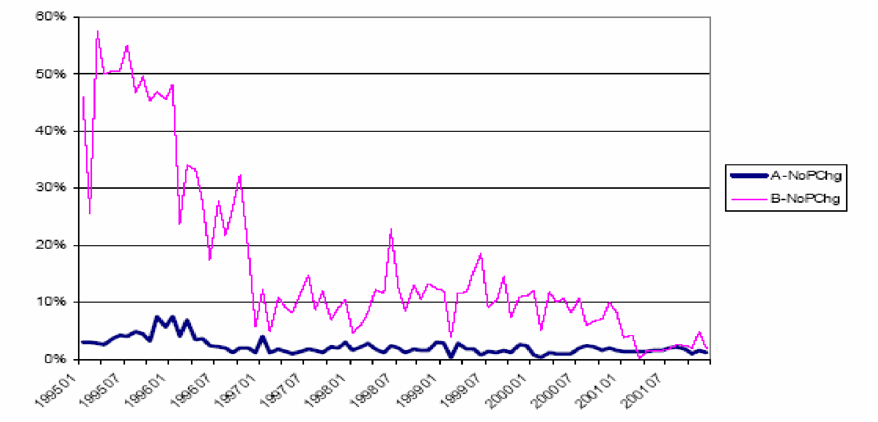
Xu and Wang (1997) adopted the Market to Book Ratio for their research. The market value ratio relates the firm's stock price to its earnings, cash flow, and book value per share. It can be used to test the confidence of investors. Generally, the liquidity, asset management, debt management, and profitability ratios all look good, then the market value ratios will be high, and the stock price will probably be as high as can be expected. According to Wang (1997) this norm does not work in Chinese marketing which has a high speculation feature.

The stocks in Chinese companies include state-owned shares, legal person shares, "A" shares and "B" shares. The state-owned shares can not be sold in the public and legal person shares generally hold for long time. So the MBR ratio will largely be impacted by "A" shares and "B" shares. If only concerning about the "A" share in the companies, speculation will make the MBR more confused. However "B" share trading is more reasonable in comparison with "A" shares because foreign investors have less information about local firms and they have less speculation (Figures, overleaf). As we can notice form the figure, the price of "B" shares has much less fluctuated during the past few periods and "A" share has high speculation in terms of price change and turnover. Because "B" share has a much lower volume traded on SSE in comparison with volume of "A" share, the meaningful impacts from "B" share will be covered by speculation and unreasonable impacts from "A" share trading. Then, the Market to Book Ratio will not be adopted in this study.

Figure 3.1.3 Shanghai "A" and "B" share price indices

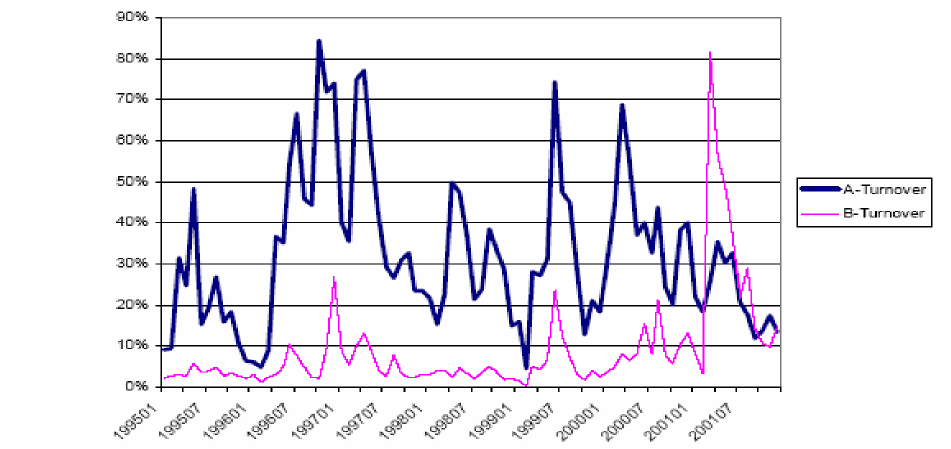
Source: Shanghai Stock Exchange Market (2005)

Figure 3.1.4 Time series of percentage change of no-price-change dates in a month for “A” & “B” share



Source: Shanghai Stock Exchange Market (2003)

Figure 3.1.5 Time series of average monthly turnover rates for “A”& “B” shares



Source: Shanghai Stock Exchange Market (2003)

Consequently, the study can not utilize MBR as one of the basic ratios to evaluate the performance of companies because of high speculation from “A” share trading.

A lot of ratios introduced by many academics, we will choose only two of them: ROE and ROA. The reason is stated as follows.

1. Almost all previous research used those two ratios to test the performance of the companies, such as Huang (2004), Qi, Wu and Zhang (1999), Wu (2004), Xu and Wang (1997), and so on. It reveals that it is meaningful to use these two ratios to test the performance of listed companies.

2. These two ratios reflect exactly the two aspects of a firm’s performance, namely, efficiency and effectiveness of using assets to generate profits, level of profitability contributed to investors.

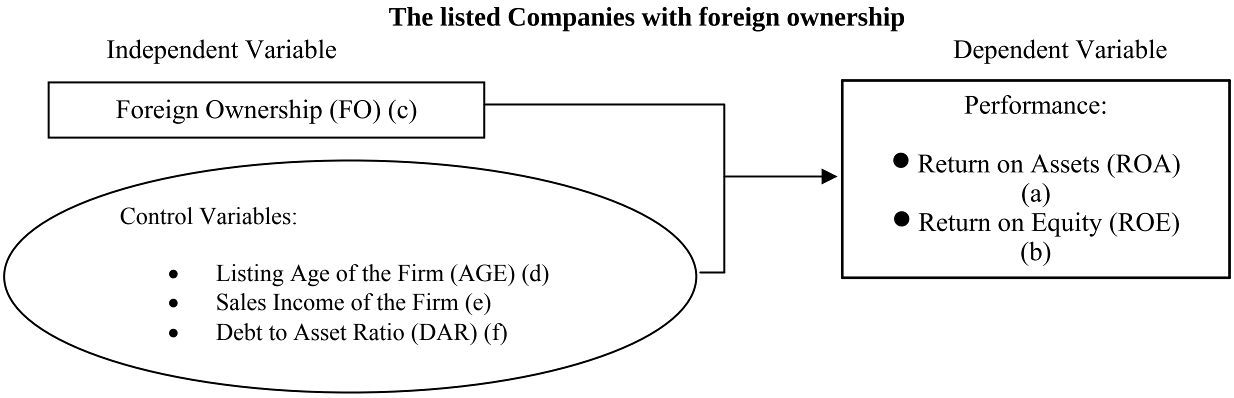
3. Since ROA and ROE calculation use net income or income available for common stock holders, therefore differentiation of tax treatment and finance leverage ability between foreign and non-foreign owned companies have been considered in the calculation of net income. However, other ratios such as Basic Earning Power Ratio (BEP), liquidity ratio and asset turnover ratio can not reflect the real practice in the Chinese market which has high differentiation toward foreign and non-foreign owned companies.

Apart from that, factors other than foreign ownership also determined the performance efficiency and effectiveness of listing companies as mentioned by prior studies of Wang (1997) and Zhang (1998). Especially, the operation period, the industry area, size effect of firms and financing structure will be considered as fundamental factors that affect the performances of the corporations in this study. This study introduces them as a set of control variables.

THE CONCEPTUAL FRAMEWORK

This research is separated into two steps: the first is to describe the characteristics of the listed companies with foreign ownership in terms of the structure of financing, performance of operation, and so on; the second is to test the relationship between the proportion of foreign ownership and performance in Chinese listed companies with foreign ownership.

Figure: Conceptual Framework



METHODS OF RESEARCH USED

According to the literature of Wu (2004) and Wang (1997), that research employed two accounting ratios to measure the firm's performance, namely, ROE, and ROA. In terms of other factors that affect the performance of the companies, a group of control variables will be introduced in this study. These major control variables influence the performance of Chinese listing companies and were considered in this research, such as the proportion of foreign shares, the listed period, financial policy and size of the companies. The reasons for selecting those factors have been explained in the previous chapters.

For this research, the data are complied with the listed companies of the Shanghai Stock Exchange of China (SSE). The methodologies of this study are descriptive statistics and regression analysis. Moreover before using regression analysis, two basic evaluations of performance ROE, and ROA were calculated respectively.

The descriptive statistics are adopted first to investigate the situations and characters of Chinese listing companies with foreign ownership. The purpose of descriptive statistics can help the study achieve concrete understanding and insights for foreign ownership companies before doing further regression analysis. In the descriptive statistics, the means of return, the proportion of foreign shares, the listed period, financial policy and size of the companies will be reflected clearly through histograms and tables. The clear scenes from descriptive statistics will somehow provide the probable answers to the results of regression analysis.

Regression analysis can be used to establish that a set of independent variables explains a proportion of the variance in a dependent variable at a significant level (through a significance test of R^2), and can establish the relative predictive importance of the independent variables (by comparing beta weights). Then this analysis can find out how foreign ownership with other controlling variables explains a proportion of the variance in performance (ROE and ROA) at a significant level.

The regression model can be written in the form as follows:

$$Y = \alpha + ß1\ FO\ it + ß2\ AGE\ it + ß2\ Sale\ it + ß3\ DAR\ it + e\ it$$

Where Y is the dependent (ROE, and ROA), the ß's are the regression coefficients for the corresponding independent terms, α is the constant or intercept, and e is the error term reflected in the residuals.

FO: foreign investment proportion in the corporate.

AGE: the ratio of listed period of a firm till observing period over average period of the firms.

Sale: the ratio of operating sales in Ren Min Bi over average operating sales of the firms.

DAR: financial leverage calculated through total debt divided by total asset.

UNIT OF ANALYSIS

The unit of analysis in this study is the population of firms that have foreign ownership and are listed in the Shanghai Stock Exchange Market (SSE).

Table 4.2.1 Selected foreign-shares companies listed on the Shanghai Stock Exchange

Industrial Sectors	Number of selected companies with foreign ownership	Number of Balance Sheets	Number of Income Statements	Number of selected financial statements
Manufacturing	29	145	145	290
Trade	10	50	50	100
Real Estate	5	25	25	50
Utility	6	30	30	60
Total	50	250	250	500

However, in this case, the populations of companies selected are only combined into 4 sectors for the purpose of avoiding insufficient information. Moreover, the data excluded companies under rehabilitation, and the companies with a listed period of less than 5 years.

SUMMARY OF FINDINGS

Overall findings showed high cautions paid by foreign investors when they make a decision to invest. They prefer listed companies with a big economic size and long operational experience. Beside that, proportion of foreign ownership was maintained at a moderate level from 25% to 50%. Industry area from foreign investment is in manufacture and very few companies from real estate industry were listed in “B” share market.

According to the findings, the financial leverage of Chinese listed companies is diversified. Some companies have very low funds raised from debt and some have much higher funds from debt. This is probably due to the different ability of borrowing from government-owned banks and other state-owned corporations.

FOREIGN INVESTED COMPANIES’ CHARACTERISTICS

1. There are some concentrations of investment. Foreign ownership prefers big economic size and long listed experience companies. Beside that, only the manufacturing industry received much attention from foreign investment.

2. Performance results in terms of ROA and ROE are quite similar, which accounts for 0% to 10% even these two ratio have different aspects. Besides some companies have a big loss of -150% and are almost bankrupt and some companies got almost 20% dramatic ROE. A majority of companies are around -10% to +10% ROA and ROE.

3. Foreign ownership of Chinese listed companies was kept at a moderate level which accounts for 25% to 50%. Very few companies have a proportion of ownership from foreign investment higher than 50% and become major shareholder of the company. Some companies only have 5%-10% foreign ownership which is much lower than other share holdings.

4. Financial leverage in Chinese listed companies is very different. Some companies have a majority fund contributed by the government bank, which almost accounts for 60% overall. And some companies got a very low debt from banks or government agencies which only accounts for 10% of overall financing. It’s probably thanks to large state ownership in the company.

SUMMARY OF HYPOTHESES TESTING

1. There is no significant relationship between foreign ownership and the performance of Chinese listed companies in terms of return on equity. The significance of relation under regression method showed higher than the defined level of 0.05. Meanwhile the relation between foreign ownership and return on equity accounts is very weak. Finally, the study shows that there is no significant relationship between foreign ownership and overall performance of Chinese listed companies in the Shanghai Stock Exchange Market.

2. There is no significant relationship between foreign ownership and the performance of Chinese listed companies in terms of return on assets. The regression method showed the significance between foreign ownership and return on equity in accounts is lower than 0.05 of the defined level. Finally, we can say there is no significant relationship between foreign ownership and efficiency and effectiveness of Chinese listed companies in the Shanghai Stock Exchange Market.

3. In one word, the relationship between foreign ownership and performance of Chinese listed companies does not exist. The relationship between foreign ownership and the efficiency and effectiveness of using assets to generate profit also does not exist. There is no relationship between foreign ownership and the performance of Chinese listed companies.

DISCUSSION AND CONCLUSION

According to the findings, foreign ownership still hesitates to make investment in small economic size and non-manufacture industrial Chinese listed companies with enough confidence. It is probably because of the belief that Chinese state ownership will not let Chinese companies down when a financial crisis and other unexpected recessions come. Foreign ownership still feels safe when they make investments in Chinese listed companies with a moderate proportion of shares which accounts for 25% to 50% and lets the state hold large shares of listed companies.

However, the situation is changing with further improvement of the Chinese economy. Except for banking and other utility industries, all unprofitable and bad management corporations owned by the state are going to be privatized. That means the Chinese central and local governments will not protect these companies any more. As a consequence, if foreign ownership still holds this belief, big losses and unexpected risks will come soon.

Anyway, with foreign ownership lower than 50% and the state holding a majority of shares of Chinese listed companies, internal efficiency and effectiveness of using asset to generate profit can be improved because of pressure from foreign ownership, even overall performance of listed companies in terms of ROE remained similar. The probable reasons are listed as follows.

1. The Chinese state maintains a majority ownership of listed companies. It means social stability and profitability become the top purpose of companies. That also means business profitability will be considered as a target of the company only after social and national welfare has been meted out.

2. As mentioned in other topics of this study, foreign ownership has claims over the assets of invested companies but no or limited voting rights over strategic decision making. In order to be listed on the Chinese "B" share market and avoid investment withdrawal by foreign ownership, and other pressure, Chinese listed companies have to improve their internal management systems and standardize their management. However, this improvement is under the supervision of the majority state share holders. Social stability is still the first consideration.

As a conclusion, there is no relationship between foreign ownership and the performance of Chinese listed companies. It is probably the reason that majority ownership is still under control of state ownership. There is a material difference and conflict in purpose and goal of foreign ownership and state ownership.

In comparison with previous researches including, Huang (2004), Qi, Wu and Zhang (1999), Wu (2004), and Xu and Wang (1997), the study gives different results when the type of ownership has been changed.

RECOMMENDATIONS FOR CHINESE LISTED COMPANIES

Because of long-term state owned experience and not-so-good management reputations, Chinese listed companies had major problem raising funds when they were trying to attract foreign ownership. In the survey of the characteristics of foreign-share companies, with big economic size, long age, and moderated foreign shares, showed that investors are still hesitating to demonstrate enough confidence to invest in Chinese listed companies.

The confidence shortage generally is because of limited participation of foreign ownership and the priorities of state-ownership. This is also because they are afraid of intervention from state or local government agencies. Then further separation of the functions and rights of business companies and government should be strongly supported.

1. Government agency ownership can not have priority over other ownership. Both state share holders and other private share holders should have the same voting and decision making rights.

2. The Chinese listed companies should keep abreast with overseas or western advanced management development. Only on the condition that internal management capability continues to be improved, foreign investors will contribute enough funds and other support without hesitating.

3. For financial leverage, the study showed that some corporations raise too funds through debt which accounts for around 60% and some corporations raise too low debt, only about 10%. These findings show that financial strategies are not working under suitable rationales, when economy cools down, the consequences will become more serious. So improvement of financial management is on the agenda.

4. According to the findings, some corporations were in a high fluctuation in terms of ROA and ROE. A healthy business organization should have stabilized profitability with on-going improvements. Then, how to stabilize income, profitability, costs and expenses, and others, should be another important task for Chinese listed companies if they want more confidence from foreign investors.

5. Try to create "immune" characters to cope with impacts from unstable government policies and regulations. With local protectionism and different treatment, companies' profitability was largely changed. The impact from the Chinese government

is unavoidable. However, Chinese listed companies should not be too weak to respond and handle changes. A system of better strategies and tactical policy for Chinese listed companies is urgently required.

RECOMMENDATIONS FOR FOREIGN INVESTERS

1. Foreign investors can not consider Chinese listed companies with, large economic size, long experience, and in the manufacturing industry only. The concentration should be on searching for listed companies with a stable performance and good management systems. Some Chinese companies have big economic size and long listing experience but still much fluctuation in terms of ROA and ROE. Unstable profitability and putting all eggs in one basket: manufacture, probably make investment more risky and return uncertain in the long term. So paying attention to small size but stable profitability should be much better. On the other hand, Chinese companies are in a development process with the Chinese economy dramatically changed every year. We should have enough confidence to believe in the potential ability of further advancement from Chinese companies with a small size and in other industry areas.

2. High speculation in the Chinese stock market still exist and state ownership still controls the management system of profit organization. Foreign investors can not have much hope for a healthy and formal return from Chinese listed companies and should be ready to accept unexpected changes from Chinese listed companies in terms of profitability and performance.

3. Although foreign investors have no significant impact on the overall performance of Chinese listed companies according to the findings of ROE, foreign ownership still can contribute enough effort to push and spur Chinese companies which are afraid of investment withdrawal. So there is something that foreign ownership still can do to protect their investment. With continued improvement of internal management efficiency and effectiveness and further liberalization of the Chinese economy, overall profitability will change and get better.

RECOMMENDATIONS FOR FURTHER RESEARCH

Because of limited data availability, only around 50 listed companies with foreign ownership in the Chinese stock market currently, the accuracy of the finding can not be guaranteed. With the further opening of the Chinese stock market and improvement of performance of Chinese listed companies, more and more Chinese firms will get into foreign shares market to attract more investment from overseas or foreign currency. Data availability will also continue to be improved. Then researchers can obtain more data to make a deeper study.

It will be appreciated if further research can continue to investigate the impact on management efficiency and effectiveness from foreign shares. The impact from foreign ownership isn’t fully brought into play. Limited participation and restrictive voting rights make foreign shareholders not give enough pressure on the management teams of listed companies. But in the future, it will be changed when unfair authority is moved away due to further economic liberalization.

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